Re-Authorize or Retire the Export Import Bank?

Testimony of

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My name is Ian Vásquez and I direct the Project on Global Economic Liberty at the Cato Institute. I would like to thank Chairman Bereuter for inviting me to testify. In the interest of transparency, let me point out that neither the Cato Institute nor I receive government money of any kind.

President George W. Bush has called for a 25 percent cut in the funding of the Export Import Bank, which provides loans, guarantees and insurance that benefit U.S. exporters. The proposed cuts are a good start, but Congress should go much further in recognition that the rationales for using Export Import Bank credit do not justify its current level of authorizations. The Bank's two main rationales—that it should provide support where the private sector does not or where U.S. exporters face subsidized competition abroad—are specious.

The Export Import Bank and its proponents cite a number of reasons, ranging from jobs created to maintaining American competitiveness, that the credit agency benefits the United States. Yet because the Bank takes resources from the U.S. economy and diverts them toward politically determined, less efficient uses, its intervention creates distortions in the national economy and imposes opportunity costs that are surely higher than the added value of the Bank's intervention.

Moreover, subsidized export credits do not create jobs nor noticeably affect the level of trade. Indeed, only about 1.5 percent of all U.S. goods and services exports are backed by the Ex-Im Bank—far too small to make an impact on trade. For that reason, those who mistakenly view the U.S. trade deficit as a sign of weakness rather than as a sign of strength should not expect the Ex-Im Bank to correct the perceived malady. As the General Accounting Office has noted, "Eximbank programs cannot produce a substantial change in the U.S. trade balance."[1] Other factors play a much larger role in influencing jobs and trade, as the Congressional Research Service recently noted.

> Most economists doubt . . . that a nation can improve its welfare over the long run by subsidizing exports. Economic policies within individual countries are the prime factors which determine interest rates, capital

flows, and exchange rates, which, in turn, largely determine the overall level of a nation's exports. This means that, at the national level, subsidized export financing merely shifts production among sectors within the economy, rather than adding to the overall level of economic activity, and subsidizes foreign consumption at the expense of the domestic economy. This also means that promoting exports through subsidized financing or through government-backed insurance guarantees will not permanently raise the level of employment in the economy, but it will alter the composition of employment among the various sectors of the economy.[2]

Thus, the Bank benefits particular firms and their shareholders at the expense of taxpayers and the vast majority of U.S. exporters that do not receive the agency's subsidies. When the "market failure" and "level playing field" rationales of Ex-Im Bank finance are also scrutinized, reasons to fund this example of corporate welfare are difficult to find.

Government Credit and the Market

A principal rationale for use of Ex-Im Bank resources is that the agency provides its services when the private sector is unable or unwilling to do so on its own due to perceptions of excessive risk. Yet the Bank has been providing the bulk of its loans, guarantees and insurance to countries such as China, Mexico, and Brazil that have had little difficulty attracting private investment on their own. As Table 1 shows, 10 countries account for 50 percent of the agency's total exposure. Table 2 shows that the pattern did not change in FY 2000.

Table 1
Top 10 Countries Benefiting from Ex- Im Bank
(Ex- Im Bank Exposure 9/30/00)

	Country		Exposure	Percentage of Total
1	China	$	6,197,191,835	10.06
2	Mexico	$	4,500,777,599	7.31
3	Brazil	$	3,576,223,094	5.81
4	Turkey	$	3,523,429,372	5.72
5	Indonesia	$	2,826,993,322	4.59
6	Saudi Arabia	$	2,526,989,512	4.10
7	Korea	$	2,389,778,130	3.88
8	Russia	$	2,075,983,958	3.37
9	Venezuela	$	1,833,180,504	2.98
10	Philippines	$	1,756,985,326	2.85
TOTAL		$	31,207,532,652	50.67

Total Exposure:
$ 61,595,682,783

Source: Export- Import Bank, *2000 Annual Report*

(Washington, D.C.: Export- Import Bank, 2000)

Table 2
Top 10 Countries Benefiting from Ex- Im Bank in FY2000
Total Actual Authorizations

	Country	Total Actual Authorizations	Percentage of Total
1	Mexico	$ 1,454,768,716	11.51
2	Turkey	$ 1,247,240,959	9.87
3	Malaysia	$ 837,215,177	6.63
4	Taiwan	$ 607,848,319	4.81
5	Saudi Arabia	$ 551,227,643	4.36
6	Thailand	$ 502,615,844	3.98
7	China	$ 498,339,026	3.94
8	Brazil	$ 487,064,993	3.85
9	Venezuela	$ 371,945,750	2.94
10	Korea	$ 336,629,641	2.66
TOTAL		$ 6,894,896,068	54.56

Total Authorizations:
$ 12,637,061,926

Source: Export- Import Bank, *2000 Annual Report*
(Washington, D.C.: Export- Import Bank, 2000)

In short, Ex-Im Bank activity has largely mirrored that of private credit markets. This was even so during the Asian financial crisis that disrupted trade and private credit flows, despite claims by the Bank that its lending at the time played a crucial role in the recovery of the affected countries. Rather, economist William Cline notes that only in Korea did the Bank provide much short-term credit, but that policy "was not very successful elsewhere in the region." Although the merits of such a policy are dubious, Cline adds that the agency's "longer-term operations have not been used much for systemic stability purposes and, arguably, have been pro-cyclical rather than counter-cyclical."[3]

At best, then, the Bank provides financing to countries that do not have trouble obtaining credit and in many cases merely displaces private investment by funding ventures that would otherwise have taken place. At worst, the credit agency underwrites exports that should not be financed and would not otherwise receive support. Indeed, the lack of private-sector finance on acceptable terms is not an example of market failure, but rather an important market signal about a project's prospects or a country's investment regime. In cases where the Bank provides credit into a bad policy environment, it discourages host governments from adopting market reforms necessary to genuinely attract private capital. When the policy environment is overlooked by export credit agencies, economic development begins to suffer. In 1969, the Pearson Commission, which assessed international development policies, warned of that danger.

> More than one project rejected for financing by the World Bank Group on economic grounds has been promptly financed by an export credit. This is the most unfortunate aspect of export credit finance: it provides a temporarily painless way of financing projects conceived by over-optimistic civil servants, by politicians more concerned with immediate political advantage than with potential future economic problems, and by unscrupulous salesmen for the manufacturers of capital equipment in developed countries.[4]

Of course, the result of such an approach is debt instead of development. In the worst of cases, the accumulation of debt becomes unpayable and its reduction must be financed by Western taxpayers who funded the credit agencies to begin with. The current debt relief initiative led by the World Bank and the International Monetary Fund has identified 41 highly indebted poor countries whose foreign debts cannot be repaid. In many cases, credit from official export agencies accounts for a high proportion of that external debt.[5] Since the majority of those highly indebted countries are in sub-Saharan Africa, it is especially worrisome that Ex-Im Bank has significantly expanded its operations the region in the past few years and plans to continue expanding there. Indeed, of the 14 sub-Saharan African countries that received Ex-Im Bank credit or guarantees in the past three years, all rank poorly in terms of economic freedom and 10 are on the World Bank's and IMF's highly indebted country list.

The Ex-Im Bank undermines the spread of free markets and economic development in other ways. For example, a large portion of the agency's credit finances public-sector borrowers. In 1999, 45 percent of Ex-Im credit financed the public sector.[6] Numerous loan guarantees to Mexico's state owned oil and electricity monopolies, loans to Korea's Development Bank, and loan guarantees to Air China during the past few years have certainly not accelerated the move to the market and their provision sends a contradictory message to countries where the United States presumably wishes to promote free-market reforms.

Thus, while private credit markets are not perfect, the unintended consequences of subsidized credit loom large and, as my colleague William Niskanen, former head of President Reagan's Council of Economic Advisors has observed, "Any effects of market failure are likely to be small and transient in comparison to the effects of government failure."[7] Those effects include the fact that Ex-Im Bank operations are often harmful to economic development, often displace private-sector finance, impose "potentially significant" opportunity costs,[8] finance firms abroad that compete with U.S. firms, and politicize the market by providing a few large firms with government loans and guarantees. Indeed, as Table 3 shows, the top 10 U.S. companies that benefit from Ex-Im Bank loans and guarantees receive 86 percent of those Bank services. Boeing alone accounted for 43 percent of total Ex-Im Bank loans and guarantees in FY 2000. By contrast, small businesses account for only 18 percent of all Ex-Im lending. Yet even if more lending went to small businesses, the Bank would still not be able to avoid the perverse effects that have accompanied lending to its larger clients.

In sum, if the private sector is not already providing export credit or insurance to a project, there are probably good reasons for that outcome and little reason for the Ex-Im Bank to step in. Nor should the Bank have a role if the private sector is willing to provide finance or is contemplating it.

Table 3
Top 10 U.S Beneficiaries of Ex- Im Bank Loans and Guarantees FY2000

U.S Company	Revenues*	Total (Loans & Guarantees)	Percentage of Total
1 Boeing Co.	$ 51,321	$ 3,384	43.1
2 Bechtel International	$ 14,300	$ 1,475	18.8
3 Varian Associates Inc.	$ 704	$ 674	8.6
4 United Technologies (1)	$ 26,583	$ 334	4.3
5 Willbros Engineers	$ 314	$ 200	2.5
6 Halliburton Co. (2)	$ 11,944	$ 172	2.2
7 Raytheon Engineers & Constructors	$ 16,895	$ 150	1.9
8 Enron Development Corp.	$ 100,789	$ 132	1.7
9 General Electric Co.	$ 129,853	$ 127	1.6
10 Schlumberger Technology Corp.	$ 10,034	$ 87	1.1
TOTAL		$ 6,735	85.9
GRAND TOTAL		$ 7,844	

* In millions of U.S dollars
Sources: Export- Import Bank, *2000 Annual Report* (Washington, D.C.: Export- Import Bank, 2000); and the 2000 annual reports from each of the listed companies.
Notes:
(1) The figure for United Technologies includes loans and guarantees for Sikorsky Aircraft Corp., which is a wholly owned subsidiary of United Technologies.
(2) The figure for Halliburton Co. includes loans and guarantees for Brown and Root International, Inc., which is a wholly owned subsidiary of Halliburton Co.

Using Government Credit to Level the Playing Field

The other principal rationale for Ex-Im Bank finance is to counter the subsidized competition that U.S. firms sometimes face. Although U.S. companies should not have to compete in a world where their competitors receive support from their governments, U.S. policy should be consistent with the goal of maintaining a prosperous national economy as opposed to promoting the welfare of particular groups. Fortunately, Europe and Japan are already re-appraising the utility of their export programs in light of fiscal constraints and as a reaction to each other's subsidized export policies.[9] The consistently poorer economic performances of Western European countries and of Japan in comparison to that of the United States argues against the United States adopting the types of policies—including more expensive export-finance programs—that have hindered growth in Europe and Japan.

It is important to recognize, moreover, that much Ex-Im Bank credit helps U.S. firms that do not face competition subsidized by foreign governments. In FY 1999, for example, only 18 percent of medium and long-term loan and guarantee transactions went to counter government-backed export credit competition, representing $6.3 billion of the Bank's activity. In the same year, only 15 percent of the Bank's total dollar amount of medium-term insurance, or $89 million, went to counter officially supported foreign competition.[10] Those figures suggest that the Bank could significantly reduce its activities without undermining its mission to counter foreign-subsidized competition. Because Ex-Im Bank credit to companies that do not face this type of unfair competition cannot be justified on economic grounds, the Bush administration's proposal to cut the Bank's funding by 25 percent should be viewed as a starting point even by those who believe that the agency has a legitimate role in countering subsidized foreign exports. At the very least then, the Export-Import Bank should be limited to financing exports that meet this criteria.

But the idea that the United States suffers from a playing field that is not level is questionable. The United States exports about $1 trillion of goods and services per year. The Ex-Im Bank backs only about $15.5 of that amount, or 1.5 percent of total exports, only some of which face government-subsidized competition. When only a fraction of 1 percent of U.S. exports faces competition supported by foreign export credit agencies, it is difficult to conclude that the U.S. economy is threatened by a playing field tilted against it.

Retiring the Ex-Im Bank entirely might reduce the profits of the few large corporations that have received the bulk of the agency's finance over the years. But surely firms such as Raytheon and Enron—with annual sales of more than $16 billion and $100 billion respectively—can cope in a world without Ex-Im Bank subsidies. Likewise, small business that do not have recourse to the vast financial resources of large corporations, already seem to be doing well without the Bank's help. The agency supports only 2000 small businesses, or about 1 percent of all small and medium exporting firms.

If the goal is to help U.S. exporters, there are other, preferable ways in which to do so, namely by making the United States a more competitive economy. U.S. tax levels, regulations, and the complexity of the tax code are routinely cited as factors that hinder the competitiveness of U.S. firms. As one report by Price Waterhouse found, "The U.S. system has also diverged in a number of respects from the policies and practices of other major industrial countries—often to the detriment of U.S. businesses striving to compete in foreign markets."[11] Thus, there is much Congress can do to help the business sector. I suggest it begin by eliminating the $65 billion dollars worth of corporate welfare that exists in the federal budget—of which Ex-Im Bank is a part—a move that would generate savings sufficient to eliminate the capital gains and federal estate taxes.

Conclusion

It is time Congress retire the Export Import Bank in recognition that the Great Depression-era agency has no relevance in an increasingly liberal world economy. The Bank benefits a small number of firms at the expense of the rest of us. It does not correct for so-called market failures, but does create perverse effects at home and abroad, including by imposing opportunity costs and discouraging the spread of market reforms. The tiny percentage of exports that the Ex-Im Bank helps to counter subsidized competition overseas, moreover, demonstrates that the U.S. economy does not suffer from the lack of a level playing field. Most important, Congress should not finance this negative sum game because it is nowhere authorized in the Constitution to use taxpayer funds to benefit politically favored groups.

Notes

[1] Jay Etta Hecker, "Export-Import Bank: Key Factors in Considering Eximbank Reauthorization," Testimony before the Subcommittee on International Finance of the Committee on Banking, Housing, and Urban Affairs of the U.S. Senate, July 17, 1999, p. 6. For a review of the current trade deficit, see Daniel T. Griswold, "America's Record Trade Deficit: A Symbol of Economic Strength," Cato Institute Trade Policy Analysis no. 12, February 9, 2001.

[2] James K. Jackson, "Export-Import Bank: Background and Legislative Issues," Congressional Research Service Report for Congress 98-568E, January 19, 2001, p. 5.

[3] William R. Cline, "Ex-Im, Exports, and Private Capital: Will Financial Markets Squeeze the Bank?" in Gary Clyde Hufbauer and Rita Rodriguez, eds., *The Ex-Im Bank in the 21st Century: A New Approach?* (Washington: Institute for International Economics, 2001), p. 102.

[4] Lester B. Pearson, *Partners in Development: Report of the Commission on International Development* (New York: Praeger, 1969), quoted in Patricia Adams, *Odious Debts* (Toronto: Earthscan, 1991), pp. 84-5.

[5] See Friends of the Earth et al., "A Race to the Bottom: Creating Risk, Generating Debt, and Guaranteeing Environmental Destruction," March 1999, p. 35.

[6] John Lipsky, "Can Trade Finance Attract Commercial Banks?" in *The Ex-Im Bank in the 21st Century*, p. 207.

[7] William A. Niskanen, "Should Ex-Im Bank be Retired?" in *The Ex-Im Bank in the 21st Century*, p. 193.

[8] "Export-Import Bank: Background and Legislative Issues," p. 5.

[9] Peter C. Evans and Kenneth A. Oye, "International Competition: Conflict and Cooperation in Government Export Financing," in *The Ex-Im Bank in the 21st Century*, pp. 154-55.

[10] Export-Import Bank, *2000 Annual Performance Report*, chapter 1, pp. 2-3, available at: http://www.exim.gov/annperf00.html.

[11] Price Waterhouse, "Taxation of U.S. Corporations Doing Business Abroad: U.S. Rules and Competitiveness Issues." See also National Foreign Trade Council, "The NFTC Foreign Income Project: International Tax Policy for the 21st Century," NFTC, March 25, 1999 and testimony of Bob Perlman (Intel Corporation) before the Senate Finance Committee, March 11, 1999. Perlman states that "If I had known at Intel's founding . . . what I know today about the international tax rules, I would have advised that the parent company be established outside the U.S. This reflects the reality that our Tax Code competitively disadvantages multinationals simply because the parent company is a U.S. corporation."